



Aflac Inc. (AFL)

Updated July 26th, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$54	5 Year CAGR Estimate:	3.0%	Volatility Percentile:	3.3%
Fair Value Price:	\$42	5 Year Growth Estimate:	6.0%	Momentum Percentile:	69.5%
% Fair Value:	129%	5 Year Valuation Multiple Estimate:	-5.0%	Growth Percentile:	53.0%
Dividend Yield:	2.0%	5 Year Price Target	\$56	Valuation Percentile:	23.1%
Dividend Risk Score:	A	Retirement Suitability Score:	B	Total Return Percentile:	19.2%

Overview & Current Events

Aflac Inc., founded in 1955, is the world's largest underwriter of supplemental cancer insurance. The diversified insurance corporation also provides accident, short-term disability, critical illness, dental, vision, and life insurance. Roughly 70% of the company's pretax earnings are derived from Japan, with the remaining 30% coming from the United States. The company has increased its dividend for 36 consecutive years. With a market cap of \$40 billion, Aflac generates \$3 billion in annual profits.

On July 25th, 2019 Aflac released Q2 2019 results for the period ending June 30th, 2019. For the quarter the company reported \$5.51 billion in revenue, a 1.4% decrease from the \$5.59 billion reported in Q2 2018. Net earnings totaled \$817 million or \$1.09 per share, compared to \$832 million or \$1.07 previously. However, this quarter includes net realized losses, whereas the previous quarter had net gains. On an adjusted basis, earnings-per-share came in at \$1.13, representing a 5.6% year-over-year increase. For the past six months, total revenue increased 1.0% to \$11.2 billion, while net earnings of \$1.7 billion (\$2.32 per share) increased from \$1.6 billion (\$1.98 per share).

In addition, Aflac also reiterated its outlook for 2019. The company expects share repurchases to be in the \$1.3 billion to \$1.7 billion range and has an objective of generating \$4.10 to \$4.30 in adjusted earnings-per-share.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$1.96	\$2.57	\$2.09	\$2.93	\$3.09	\$3.08	\$3.08	\$3.40	\$3.41	\$4.17	\$4.20	\$5.62
DPS	\$0.56	\$0.57	\$0.62	\$0.67	\$0.71	\$0.75	\$0.79	\$0.83	\$0.87	\$1.04	\$1.08	\$1.40
Shares	937	939	933	936	919	885	849	812	781	755	740	690

From 2007 through 2018, Aflac was able to grow earnings-per-share by an average compound rate of 8.8% per annum, although part of that improvement is tax reform related. Also, keep in mind that from 2011 through 2017 the Yen was generally weakening against the dollar. For 2019 the company has told investors to anticipate somewhere between a 1.7% decline and a 3.1% improvement on the bottom line. Our intermediate-term growth expectation is in-between the company's historical growth rate and its short-term expectations, coming in at 6% per annum.

Aflac has two sources of revenue: income from premiums and income from investments. On the premium side, this is generally sticky with policy renewals making up the bulk of income. However, Aflac operates in two developed markets where we would not anticipate seeing outsized growth in the business. The other lever available is on the investment side, where the vast majority of the portfolio is in bonds. Here there is a possibility for income improvement should rates rise in the future, although this is certainly not guaranteed. Finally, the share repurchase program has been active, which we believe is prudent considering the security's valuation.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	8.8	9.9	11.3	7.9	9.4	10.0	10.0	10.0	11.4	10.8	12.9	10.0
Avg. Yld.	3.3%	2.3%	2.6%	2.9%	2.4%	2.4%	2.6%	2.5%	2.2%	2.3%	2.0%	2.5%

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Over the last decade shares of Aflac have traded hands with an average P/E ratio of roughly 10 times earnings. We believe this is more or less fair for the security, considering that many insurers trade at a comparable multiple. While this does not make for a compelling valuation story, it is not necessarily a terrible thing as it allows for a robust share repurchase program to be more effective. Ongoing owners are much better served if the company is buying out past partners at 10 times earnings as compared to say 15 or 20 times earnings. That being said, the current valuation implies a material headwind to total return prospects.

Aflac is a Dividend Aristocrat with a long streak of rising dividends. Moreover, with the company only paying out a fourth of its profits in the form of a dividend, there is ample runway for the dividend streak to continue.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	29%	22%	30%	23%	23%	24%	26%	24%	26%	25%	26%	25%

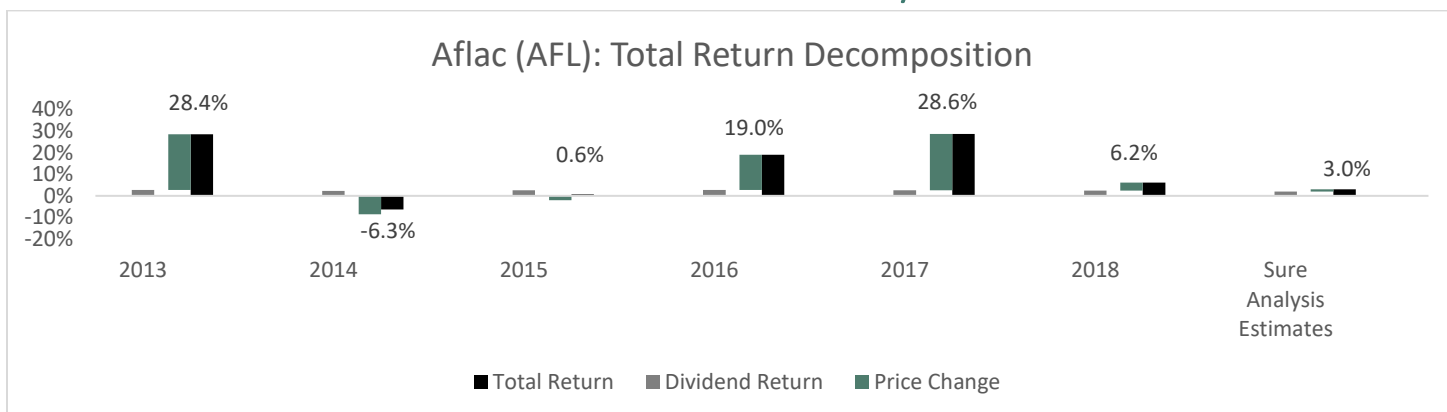
During the last recession Aflac generated earnings-per-share of \$1.64, \$1.31, \$1.96 and \$2.57 during the 2007 through 2010 period. Furthermore, the dividend was increasing this entire time. We are encouraged by the past performance and ongoing financial stability, as the company's strong brand and conservative approach serve as complementary competitive advantages. Although we do note that the company's international exposure, while strong in Japan, mitigates some of its reliability, especially as it relates to currency fluctuations.

Despite this reasonable recession performance, especially in comparison to other financial institutions, Aflac's share price dropped all the way from \$34 in the middle of 2008 down to under \$6 per share at the depths of the recession – even though the underlying earnings power was fine and the dividend never faltered. We suppose this is a general cautionary note: in the long run business results will prevail, but in the short-term anything can happen, so it's important to be prepared accordingly.

Final Thoughts & Recommendation

Shares are up 10% since our last update, while earnings expectations remain unchanged. Aflac is the sort of security that looks quite interesting from first glance, given the solid business model, great dividend growth record and starting valuation near 13 times earnings. Yet since the financial crisis shares have not traded above the current valuation very often. As such, we see total return potential of just 3.0% per annum, as the 6% growth rate and 2% starting dividend yield could be offset by a 5% yearly valuation headwind. Should shares start trading at say 13 or 15 times earnings, our expectations will be too cautious. However, for now we are uncomfortable speculating on a higher multiple and would wait for a more compelling valuation. We continue to rate Aflac as a hold at the current quotation.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	18254	20658	22090	25272	23827	22606	20811	22489	21600	21758
Net Profit	1497	2328	1937	2866	3158	2951	2533	2659	4604	2920
Net Margin	8.2%	11.3%	8.8%	11.3%	13.3%	13.1%	12.2%	11.8%	21.3%	13.4%
Free Cash Flow	6161	6989	10842	14952	10547	6550	6776	5987	6128	N/A
Income Tax	738	1233	1013	1436	1658	1540	1329	1408	-586	1063

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets (\$B)	84.11	101.04	116.24	131.09	121.31	119.77	118.26	129.82	137.22	140.41
Cash & Equivalents	2323	2121	2249	2041	2543	4658	4350	4859	3491	N/A
Accounts Receivable	764	661	680	976	1165	842	705	669	827	N/A
Total Liab. (\$B)	75.69	89.98	103.29	115.12	106.69	101.42	100.55	109.34	112.62	116.94
Accounts Payable	483	191	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Long-Term Debt	2599	3038	3275	4343	4891	5268	4951	5339	5267	5778
Shareholder's Equity	8417	11056	12946	15978	14620	18347	17708	20482	24598	23462
D/E Ratio	0.31	0.27	0.25	0.27	0.33	0.29	0.28	0.26	0.21	0.25

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	1.8%	2.5%	1.8%	2.3%	2.5%	2.4%	2.1%	2.1%	3.4%	2.1%
Return on Equity	19.9%	23.9%	16.1%	19.8%	20.6%	17.9%	14.1%	13.9%	20.4%	12.2%
ROIC	15.5%	18.5%	12.8%	15.7%	15.9%	13.7%	10.9%	11.0%	16.5%	9.9%
Shares Out.	937	939	933	936	919	885	849	812	781	775
Revenue/Share	19.46	21.83	23.53	26.93	25.49	24.90	24.02	27.17	27.07	28.09
FCF/Share	6.57	7.39	11.55	15.93	11.28	7.21	7.82	7.23	7.68	N/A

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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